STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Bell Telephone Company	)	
	)	
Application for Review of Alternative Regulation Plan	)	Docket No. 98-0252
Petition to Rebalance Illinois Bell Telephone Company's Carrier Access and Network Access Line Rates	)	Docket No. 98-0335
Citizens Utility Board and People of the State of Illinois, ex rel. James E. Ryan, Attorney General of the State of Illinois, Complainants	)	
vs.	)	Docket No. 00-0764
Illinois Bell Telephone Company d/b/a Ameritech Illinois, Respondent	)	(consolidated)

GCI / CITY REPLY BRIEF ON EXCEPTIONS

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GCI/CITY REPLY BRIEF ON EXCEPTIONS

The Citizens Utility Board, the People of the State of Illinois, ex rel. James E. Ryan, the Cook County State's Attorney's Office, (Government and Consumer Intervenors,) and the City of Chicago submit the following Reply Brief on Exceptions. GCI/City respond to the Exceptions and Brief on Exceptions of Ameritech, Illinois ("AI"), the Staff of the Illinois Commerce Commission ("Staff"), AT&T Communications of Illinois ("AT&T") and McLeodUSA.

I. THE FINAL ORDER MUST ADDRESS THE ISSUES THE COMMISSION DESIGNATED AS CRITICAL IN THE ORIGINAL PRICE CAP ORDER.

In its Exceptions, AI recommends that the Commission drop the discussion of all of the 10 issues that it directed AI to address in this review proceeding except universal service. AI Exc. at 1-2; AI Brief on Exc. p. 4, n. 2. This recommendation should be rejected. An evaluation of the Plan's performance over the past 6 years is crucial to an understanding of how the Plan has operated and what should be done in the future. A failure to address the issues the Commission identified as worthy of consideration would eliminate effective review and deny the Commission and the public the benefit of experience and hindsight.

AI suggests that the issues the Commission designated for review duplicate the issues raised in connection with whether the Plan should be modified. Although there is some overlap, it is necessary and wise to review the existing Plan and the 10 points the Commission specifically requested AI to address before determining where changes need to be made.

II. AI'S DISCUSSION OF THE RELEVANCE OF EARNINGS SHOULD BE REJECTED.

The question of how AI's earnings should be treated has been a major issue in this docket. AI maintained in its testimony and Initial and Reply Briefs that earnings were irrelevant. Staff appeared to be of two minds on the issue, offering extensive testimony on AI's earnings and cost of capital as well as policy testimony to the effect that earnings should not be a factor. The GCI/City parties have consistently maintained that a review of earnings is essential to any evaluation or review of the Plan.

In its Reply Brief, Staff argued that earnings should be considered by the Commission, and that earnings outside a "zone of reasonableness" show that rates are not fair, just and reasonable as required by section 13-506.1(a)(6); (b)(2); (e). Staff Reply Brief at 7-8. In its Brief on Exceptions, AI now concedes that "the Commission could view extraordinarily high earnings as an early warning signal that some component of the Plan may have malfunctioned, thereby warranting further review." AI Brief on Exc. at 8. While acknowledging that earnings are in fact relevant to a review of the Plan, AI then suggests that in this review proceeding, earnings are not relevant. Id. Despite AI's disclaimer that earnings are not relevant in this proceeding, it is noteworthy that at this stage of the proceeding, the hearing examiners, Staff, GCI/City and the Company all agree that earnings are relevant in reviewing performance under an alternative regulation plan. If earnings are to be reviewed at some point, this review proceeding is plainly the only and the most appropriate forum for such a review.

AI argues that in evaluating whether its rates are "fair, just and reasonable," the Commission should conclude that if the prices decreased to the extent required by the Plan, rates are by definition fair, just and reasonable. AI Brief on Exc. at 6. However, the fact that prices decreased as a result of the plan, in and of itself, does not show anything other than that the mechanics of the price cap plan were followed and the Plan operated as intended to decrease rates. It does not show whether the resulting rates are "just and reasonable" or whether the rates are within a "zone of reasonableness" when considered in light of AI’s statement of operating income. GCI/City discussed in detail how an earnings review should be incorporated into this docket to insure that AI's rates are fair in their Brief on Exceptions at 10-21(just and reasonable rates); 43-54 (rate reinitialization). GCI/City established that it is incorrect to try to consider revenues from services classified as competitive separately from non-competitive service rates and revenues that are subject to the price cap. See also Staff Ex. 18.0 at 7. Rather, the key questions are: has competition provided enough consumer protection to replace regulation and constrain prices and profits for services classified as competitive, and did the price cap formula capture a sufficient portion of AI's realized savings so that prices and profits have remained reasonable?

AI suggests that if the Commission reviews revenues, it should limit its review to AI's presentation of its financial data, and not consider adjustments recommended by GCI/City witnesses and Staff witnesses. AI Brief on Exc. at 9. As discussed in the earnings review section of GCI/City's Exceptions, pages 137-186, there were substantial errors in AI's presentation, including mistakes in the depreciation expense which the Company acknowledged. See, e.g., AI Ex. 7.3 at 1 (Dominak). Other adjustments were based on policy and regulatory principles and precedent (e.g. directory revenues, service quality adjustment) and on generally accepted accounting practices. See GCI/City Ex. 6.0 and 6.1(Smith); GCI/City Ex. 8 and 9 (Dunkel); Staff Ex. Staff Ex. 4, 18, 29 (Marshall); 5, 19, 30 (Voss); 6, 20, 31 (Hawthorn); 7, 21, 32 (Everson); The results of operations after adjustments are as "actual" as AI's presentation of its unadjusted earnings and reflect appropriate regulatory and accounting treatment of underlying costs, transactions and revenue levels.

Accordingly, the Company’s arguments in this regard should be rejected.

III. AI’S VIEW ON THE APPROPRIATE TREATMENT OF NEW SERVICES SHOULD BE REJECTED.

AI argues that its approach to new services is "consistent with the FCC's definition of new services, which the FCC had to address under the federal price cap plan." AI Brief on Exc. at 12. AI does not lay out the FCC's definition, however, and a review of the language used by the FCC demonstrates that AI's approach is not in fact consistent with the federal definition.

The FCC defined new services and restructured services in its 2000 Price Cap Order as follows:

> (i) Change in rate structure. A restructuring or other alteration of the rate components for an existing service.
>
> ...
>
> (x) New service offering. A tariff filing that provides for a class or sub-class of service not previously offered by the carrier involved and that enlarges the range of service options available to ratepayers.

> 11) Restructured service. An offering which represents the modification of a method of charging or provisioning a service; or the introduction of a new method of charging or provisioning that does not result in a net increase in options available to customers.

15 FCC Record 12962, Appendix, section 61.3. AI argues that because its calling plans offer customers choices that they did not have before, they are properly considered new services. AI Brief on Exc. at 12. This standard is at best half of the FCC definition.

The FCC definition of new services contains two requirements. First, the tariff must offer a "class or sub-class of service not previously offered by the carrier." AI does not address this requirement that the service was not previously offered by the carrier. It is only if the service is not previously available that the second requirement, that the new service enlarge service options, is triggered. See also GCI Ex. 11.0 at 61.

AI is incorrect in asserting that its application of the new services provisions of the Plan is consistent with the FCC definition. AI used the "new services" provisions to increase prices for usage despite the fact that usage is an existing service, and the calling plans did not provide for a class or sub-class of <u>service</u> not previously offered, as required by the FCC definition quoted above. Accordingly, these arguments should be rejected.

IV. AI'S CALL FOR INCREASED PRICING FLEXIBILITY SHOULD BE REJECTED.

AI argues that pricing flexibility under the Plan should be increased, and complains that it "has had essentially no flexibility to <u>increase</u> rates, even on a revenue neutral basis." AI Brief on Exc. at 14 (emphasis added). AI's argument that it should have more pricing flexibility so it can raise rates is based on several erroneous premises.

First, and most importantly, AI insists that its residential NAL rate is below cost despite the fact that the NAL rate has not been changed for over 6 years while costs have decreased substantially for the network as a whole. Second, AI's cost of service study, which purports to show a significantly higher residential NAL cost than previous studies, was found unreliable by Staff, Staff Ex. 18.0 at 4-6 (Marshall), and criticized and corrected by GCI/City witness William Dunkel to the extent that a $1.30 per line per month NAL rate decrease is justified. See GCI/City Ex. 8.0 at 13, 38-60; GCI/City Ex. 9.0 at 58-85. AI's arguments that the residential NAL rate is below cost provides no justification for pricing flexibility to increase rates because record evidence shows that the current rate is well above cost. Further, AI's argument demonstrates that given greater pricing flexibility, AI will undoubtedly increase the residential NAL rate, which is its most inelastic and essential rate.

AI argues that the existing Plan and a future Plan as recommended in the Proposed Order would leave the Company with no ability to increase pricing, and characterizes this as "excessively rigid." AI Brief on Exc. at 17. AI's costs are decreasing and earnings are increasing to the extent that its average return on equity from 1995 through 2000 of over 24%, using AI's unadjusted figures, and was 43% and 40% using GCI/City and Staff analyses, respectively. It is unreasonable for AI to expect to increase the residential NAL rate when it is the most inelastic charge, it is currently capped to promote universal service, and it currently covers LRSICs to the extent that it could be decreased by $1.30 and still cover cost. GCI/City Ex. 8.0 at 13 and 8.3.

AI further makes the misleading argument that "on an accounting basis" its book cost is $19.12, while its state-wide average residential NAL rate is only $11.81. AI Brief on Exc. at 16. The most glaring problem with this argument is that individual rates are based on long run service incremental costs, or LRSICs – not on accounting or embedded cost. The record shows that AI's residential NAL rates are at least $1.30 more than properly calculated LRSICs.

GCI/City Ex. 3.3. The correct comparison is the LRSIC for the residential NAL and the residential NAL rate.

AI did not provide record support for its $19.12 calculation. When asked to provide workpapers for this calculation, AI produced a one page, 9-line document without source references. GCI/City Ex. 9.0 at 85. Accounting or embedded costs are used to set an overall revenue requirement in traditional ratemaking, and ordinarily all revenues are combined to set rates equal to embedded costs plus a reasonable return. Therefore, if one were to compare embedded costs to rates, it would be necessary to first make the appropriate decisions on proposed adjustments, resolve cost allocation issues, and then consider whether the rates from all services that utilize the loop, such as vertical services, toll, and carrier access combine to cover embedded costs.

As the record demonstrates, overall, AI's rates produce revenues that greatly exceed its embedded costs, showing that current rates present no threat to AI's "financial viability" notwithstanding AI's insistence that the residential NAL rate is below cost. There is plenty of room to decrease rates while preserving a reasonable return for the Company based on the very accounting costs AI claims justify an increase in the NAL rate. See generally GCI/City Brief on Exc. at 15-17, 43-54.

V. THE COMMISSION SHOULD REJECT AI'S PROPOSAL TO COLLAPSE THE FOUR BASKETS INTO ONE, SINGLE BASKET.

AI continues to argue that the four baskets, established to insure that each customer class receives an equivalent benefit from alternative regulation, should be collapsed into a single basket. In light of AI's insistence that the residential NAL rate is below cost (despite the lack of support for such a position), if the four existing baskets are collapsed into one it cannot be doubted that the residential NAL rate will be increased to the maximum amount possible. This could result in violation of section 13-506.1(b)(7), which provides that alternative regulation "will not unduly or unreasonably prejudice or disadvantage any particular customer class, ..." 220 ILCS 5/13-506.1(b)(7).

If the four baskets are merged into one, residential consumers will most likely see yearly price increases, regardless of whether the Company experiences significant cost savings. As the Commission stated in the original Alt Reg Order:

> [Yearly price increases are] difficult to reconcile with our determination of just and reasonable rates using the traditional ROR regulation analysis. Under traditional ROR regulation, once rates are established they can reasonably be expected to remain in effect for several years. Under Illinois Bell's original proposal, the rate reduction we have ordered would be overtaken quickly by rate increases through the operation of the price regulation formula. **Therefore, replacing traditional ROR regulation with a formula that would provide the Company with almost automatic annual rate increases would not offer the ratepayer any readily apparent advantage**.

1994 Alt Reg Order at 41 (Emphasis added). By maintaining the existing basket structure, the Commission protects all classes of customers, including consumers of the residential NAL rate, from "almost automatic annual rate increases."

In connection with the baskets, Staff and AI attempt to incorporate the recent changes to Illinois' telecommunications law. The new law requires AI to offer three residential, flat rate packages. HB 2900, section 13-518 (new). These three packages, defined as non-competitive, are expressly intended to "result in savings for the average consumer." Two of these three baskets must include 2 vertical services. The question presented by Staff is in which service basket these services should be placed.

Should the Commission determine it is necessary or appropriate to address these statutory packages in this docket, GCI/City recommend that the statutory flat rate packages be placed in a separate, "statutory" basket. When the Plan was initially established, vertical services were in the Other basket and access and usage were in the Residence basket. Yet section 13-518 requires that two of the three packages include both of these categories of services. Further, HB 2900 defined all vertical services except Call-waiting and Caller-ID as competitive as of June 1, 2003. HB 2900, section 13-502.2(c)(new). Therefore, some packages will contain services that would normally fall in the Residential basket, other services that would normally fall in the Other basket, and still other services that are not subject to the price index at all. It is apparent that the underlying services contained in two of the three packages will fall in both the competitive and non-competitive categories and the Other and Residential baskets. Clearly, these packages do not nearly fit into any particular, existing basket.

Staff recommends that the packages be placed in the Residential basket because there is less possibility for AI to raise the prices for the packages, while still complying with the price index. Staff Brief on Exc. at 40. Although Staff does not explain its rationale in detail, it appears that Staff believes that if the packages are placed in the Residential basket, AI cannot raise the prices for the packages without lowering residential access and usage rates, whereas if the packages are in the Other basket, the package prices can be raised and the offsetting price reductions can be spread over a broader group of services which have more elastic demand (i.e. three way calling, automatic call back, order change charges etc.).

Staff's approach assumes that AI will attempt to raise the price of the packages. However, it is equally possible that AI may decrease the price of the packages as a means to increase the residential NAL rate. Further, both Staff and GCI/Staff have argued that new pricing for existing services should be subject to the pricing constraints of the basket in which the underlying services are found. Under that approach, the budget package would plainly belong in the Residence basket, but the "flat rate package" and the "enhanced flat rate package", which contain Residence services, Other services and competitive services, would not belong in any particular basket despite the General Assembly's designation of these packages as noncompetitive.

As recommended by GCI/City, a separate, statutory basket addresses the fact that these new packages include services from more than one basket. The initial price of the packages must be "at prices that will result in savings for the average consumer," HB 2900, Section 13-518(a), and therefore the price protections of the Plan are not necessary to set the initial price. If the packages are mixed with other services in one of the existing baskets, however, the prices of the packages can be modified every year so that they no longer "result in savings for the average consumer" because overall price increases to the packages could be offset by price decreases in other services. If the packages are in the Residence basket, AI could pursue a pricing strategy to raise the NAL rate so that consumers are driven to the packages even if they do not suit their needs. On the other hand, if the company increases the package prices while increasing, for example, volume discounts, the legislative intent that the packages result in savings would be thwarted.

Accordingly, GCI/City recommend that if the Commission determines how the statutory packages should be treated in its Order in this Docket, it designate a separate "Statutory" basket for them.

VI. IN DETERMINING THE TREATMENT OF MERGER SAVINGS, THE COMMISSION SHOULD ADOPT AN APPROACH THAT INSURES THAT MERGER SAVINGS ARE SHARED WITH CONSUMERS ON A TIMELY BASIS, AND THAT APPROPRIATE INCENTIVES ARE CREATED.

In evaluating the recommendations about merger savings, GCI/City urge the Commission to bear in mind the incentives and effects of the Merger Order, the Annual Rate Filing Orders, and this Order. To date, consumers have not received any merger related savings, and the first proceeding initiated to review actual merger costs and savings (ICC Docket 01-0128) has been stalled due to Ameritech's objection to paying the auditor's litigation expenses. See Order on Reopening, ICC Docket 00-0260. Further, the Hearing Examiners' Proposed Order in the 2000 Annual Rate Filing (ICC Docket 01-0302) recommended that no savings be passed through to consumers until the litigation over the audit is finally resolved, thereby allowing AI to retain all merger savings while litigation proceeds. This creates a perverse incentive for AI to delay resolution of the merger savings review dockets, and withholds the benefits of the merger from consumers, contrary to the Commission's clear intent in the Merger Order.

In the event that the Commission rejects GCI/City's approach and adopts the approach of Staff or Ameritech on how and when a permanent, going-forward adjustment should be made to the price cap formula, GCI/City maintain that the merger savings identified in the annual rate filings should be passed through to consumers annually, subject to annual true-up. This will insure that consumers receive timely benefit of merger savings, as the Commission intended, and will provide AI with the appropriate incentive to address merger savings issues. Sharing merger savings with consumers during the period before Staff's or AI's proposed permanent going forward adjustment is made will preserve the Commission's intent that merger savings be shared with consumers on an annual basis pending development of a permanent price cap adjustment.

VII. AI'S ATTEMPT TO WITHDRAW ITS RATE REBALANCING PROPOSAL IS NOTHING MORE THAN AN ATTEMPT TO AVOID THE ISSUANCE OF SPECIFIC COMMISSION FINDINGS THAT REJECT ITS COST OF SERVICE STUDIES, AND SHOULD BE REBUFFED.

In its Brief on Exceptions, AI states it is withdrawing its rate rebalancing petition from Commission consideration in this docket. AI Brief on Exceptions at p. 41. Ameritech states that it is basing its decision to withdraw the petition on the fact that pending legislation will require Ameritech to offer certain flat rate service packages to residential customers. Id. AI then asserts that it has not analyzed the impact, if any, that this legislative requirement will have on its rate structure generally, and on its rate rebalancing proposal in particular. Ameritech thus believes it would be prudent to withdraw its petition. Id.

GCI and the City vehemently oppose any attempt by Ameritech to avoid an unfavorable ruling based on the record in this docket, and request that Ameritech's attempt at unilateral withdrawal of its rate rebalancing petition be denied. Ameritech has no legal or factual basis on which to withdraw its petition. Ameritech is simply attempting to avoid an adverse decision on the merits under the pretense that pending legislation somehow affects the propriety of the Commission issuing a decision on its petition. Moreover, the parties have litigated the rate rebalancing proposal at great expense. The parties are entitled to a ruling based on the evidentiary record developed.

It must be noted that Ameritech is not requesting approval from the Commission to withdraw its petition. Apparently, Ameritech is under the impression that it has the unfettered right to withdraw its petition unilaterally despite the fact that evidentiary hearings have been concluded, the case has been submitted to the fact-finder and a preliminary determination has been made denying its petition.

Ameritech is wrong. Commission approval is necessary. Voluntary dismissal in civil proceedings, which is essentially the relief Ameritech seeks, is governed by Section 5/2-1009 of the Illinois Code of Civil Procedure. This section states, in part, that:

> After trial or hearings begins, the plaintiff may dismiss, only on terms fixed by the court (1) upon filing a stipulation to that effect signed by the defendant, or (2) on motion specifying the ground for dismissal, which shall be supported by affidavit or other proof.

735 ILCS 5/2-1009(c).

Although the Commission's Rules of Practice does not expressly incorporate Section 5/2-1009, as it does with other sections of the Illinois Code of Civil Procedure, GCI and the City submit that adoption of the standards embodied in Section 5/2-1009 is consistent with the Commission's Rules and sound regulatory policy. Since GCI and the City oppose voluntary dismissal of the petition, Ameritech should, at a minimum, file a motion establishing reasonable grounds for the dismissal. Only if the Commission finds that dismissal is proper may a dismissal be granted, and then subject to terms fixed by the Commission.

GCI and the City submit that given the fact that extensive hearings have not only begun but have been concluded, and the Examiners have already considered the evidence of record and issued a preliminary finding rejecting the petition, Ameritech cannot establish any set of facts that would outweigh the prejudice to the other parties in this case and justify dismissal at this stage. Certainly, Ameritech's vague references to the pending legislation the Company states it has not yet analyzed is not sufficient justification to fail to issue a decision on the merits based on a fully developed record. Moreover, such an extraordinary step would be inconsistent with the Commission's own Rules of Practice. See 83 Ill. Ad. Code Section 200.25.

Based on Ameritech's Brief on Exceptions, it is far from clear what impact the flat rate service packages could possibly have on Ameritech's long standing desire to raise the residential network access line rate. Ameritech cannot expect the Commission and the parties to believe that anything, including the flat rate service package requirements of HB 2900, would change Ameritech's position that the residential NAL rate should be increased. However, even if it did, a decision in this case is still warranted. Indeed, if the Commission considers the various scenarios resulting from Ameritech's "full" analysis of the impact of the HB 2900 flat rate service packages, it must come to the logical conclusion that a decision in the current case is in the public interest and more consistent with Commission policy than dismissal. This is true whether the Commission grants or denies Ameritech's rate rebalancing petition in this docket.

To illustrate, if Ameritech concludes after its analysis that the creation of flat rate service packages makes an increase in the NAL rate unnecessary, the Commission's denial of Ameritech's rate rebalancing petition will be of no consequence. If the Commission rejects the Hearing Examiners' recommendation and approves rate rebalancing, GCI and the City would not oppose any effort by Ameritech to voluntarily delay raising residential customers' rates until Ameritech has had ample opportunity to fully analyze the impact of the legislation (and the GCI/City Intervenors have had an opportunity to obtain final appellate review of that Commission decision). If Ameritech then decides that the NAL rate increase should not be implemented, GCI and the City would not oppose that decision.

On the other hand, should the Commission permit AI to withdraw its current petition and AI concludes that residential NAL rates still need to be increased even after the creation of the flat rate service packages required by HB 2900, the parties will once again have to litigate the petition at great and unnecessary expense. This violates every notion of judicial economy.

Clearly, the prospect that the flat rate service packages will somehow impact Ameritech's strategic plan to raise the residential NAL rate is a convenient smokescreen for Ameritech to avoid an adverse decision in this case. This practice has been condemned by the Illinois Supreme Court and should not be condoned by this Commission. See Gibellina v. Handley 127 Ill. 2d 122, 535 N.E. 2d 858 (1989).

The structure of the instant docket is the result of a Commission decision to consolidate Ameritech's petition for rate rebalancing with its application for review of the alternative regulation plan, and later, with the CUB/AG complaint to reduce Ameritech's rates. Having concluded that the consolidated dockets raised similar questions of law and/or fact, the Commission ordered that evidence on all three matters be taken at the same time and that the issues for all three dockets be considered simultaneously. AI cannot now unilaterally dismantle that consolidation. The Commission used its discretion to structure this docket in the manner it deemed appropriate and Ameritech has no legal or factual basis to interfere with that decision.

Furthermore, evidence has been submitted in this consolidated docket that is relevant in all three proceedings. Ameritech's summary discussion of its decision to withdraw its petition does not address what would happen to evidence submitted by the parties in connection with that petition or whether issues raised by the petition would still be subject to a formal determination by the Commission. GCI and the City maintain that as a result of the consolidation, all evidence must remain as part of the record and all issues raised by the petition must be ruled upon.

The Commission's Rules of Practice require that Commission discretion shall be exercised to ensure integrity of the fact-finding process, fairness and convenience to the parties, expeditious process, and minimization of costs to the parties and the Commission. See 83 Ill. Ad. Code Section 200.25. None of these goals would be furthered by the dismissal of

Ameritech's rate rebalancing petition. In any case, AI has made no effort to provide the evidentiary basis required by law as a condition precedent to any withdrawal of its petition at this stage of the case.

VIII. AI'S EXCEPTIONS TO THE HEPO'S COST OF SERVICE CONCLUSIONS SHOULD BE REJECTED.

Ameritech's calculation of the LRSIC for the residential access line (NAL) is seriously flawed as demonstrated by City/GCI and the Staff in their briefs, and accepted by the Hearing Examiners in the Proposed Order. These flaws permeated several facets of the Company's process including use of the ill-designed LFAM and ARPSM models as well as the inclusion of costs (i.e. billing costs) that should not be fully allocated to the NAL LRSIC.

In this regard, the City and GCI agree with Ameritech that the HEPO should be modified to clarify that many of the flaws identified in the HEPO as being related to the LFAM model should be appropriately identified as being flaws with the ARPSM model. To assist the Hearing Examiners in this effort, GCI and the City direct the Hearing Examiners to the Proposed Order language supplied by GCI and the City with their previously filed Exceptions. This language fully analyzes the numerous flaws with Ameritech's LRSIC calculation based on the record and would support the Hearing Examiners' proper and correct conclusion on this issue. Before GCI and the City addresses Ameritech's arguments regarding these additional flaws in Ameritech's LRSIC calculation, GCI and the City will respond to Ameritech's contentions regarding its LFAM model.

A. AI's Attempt to Resurrect the Flawed LFAM Model Should Be Rejected.

In its Brief on Exceptions, Ameritech attempts to resurrect its LFAM model through the use of extra-record testimony, in an effort to demonstrate that the model is based on "least cost currently available technology", as required by the Commission's cost of service rules. *See* 83 Illinois Administrative Code Subchapter f, Part 791, Section 791.20(c). GCI and the City submit that this effort fails, and the Commission should find that the record shows that the LFAM model is designed in violation of its cost of service rules. GCI and the City have submitted language reflecting this finding in its previously filed Exceptions.

Specifically, on cross examination, when asked if Ameritech's network uses an integrated technology <u>with fiber feeders</u> that does <u>not</u> require a COT in the central office (co-COT), Ameritech witness Palmer testified that it did. Tr. 1343. (Emphasis added) Despite the fact that the question to Mr. Palmer was prefaced with the following statement by counsel for the City, "Mr. Palmer, I'm sorry one last question on fiber feeder technology." (Tr. 1342), counsel for Ameritech now assert with what amounts to extra-record testimony that, "Contrary to the City's suggestion, however, Mr. Palmer was <u>not</u> referring to an integrated DLC using a <u>fiber feeder</u>. Instead, Mr. Palmer was referring to the older <u>copper</u>-based integrated DLC technology...". AI Br. at p. 57 (Emphasis in original). This extra-record self-serving "explanation" of what Mr. Palmer meant by his answer is directly contradicted by the record and must be disregarded by the Commission.

This admission by Mr. Palmer is critical because, as Ameritech readily admits, the LFAM model assumes the use of a central office COT when using integrated technology with fiber feeders. AI Br. at p. 56; Tr. 1340-1341. Since, the LFAM model assumes the cost of a component that Ameritech witness admits is neither needed nor used by Ameritech, the LFAM model is not in compliance with the Commission's cost of service rules that require "least cost currently available technology".

B. Additional LRSIC Errors

1. Common Switching Costs

To the extent that Ameritech's Brief on Exceptions implies that the City argued that common switching costs were improperly included in the LRSIC calculation of the residential NAL as a result of flaws in the LFAM model, the Company is incorrect. See AI Br. at p. 58. The City never made this argument. See City Initial Brief at pp. 62-63.

In its Brief on Exceptions, Ameritech simply restates its vague and unverifiable explanation of how it purportedly excluded improper usage and associated common costs in its NAL LRSIC calculation. AI Br. at 58. This explanation is not credible and should not be accepted by the Commission.

Ameritech's description of its methodology does not demonstrate that all of the common costs were excluded. Ameritech admits that the switch price it used to begin its analysis is bundled on a single per-line basis that includes all line-related, usage-related, and common related hardware and software. AI Br. at 59. Ameritech then refers to some "additional information" that Ameritech requested from the switch vendors that allowed it to "implicitly" identify the usage component of the total per-line cost Id. Ameritech then makes the following assumption, without any basis, that "any costs associated with common equipment that are inherent in the single per-line prices of the vendors are, by default, assigned to lines and usage in proportion to their respective implicit costs." Id. This indicates that Ameritech is still including common costs in the port costs.

Accordingly, Ameritech's recommended exception language should not be accepted.

2. Network Interface Device (NID)

To the extent that Ameritech's Brief on Exceptions implies that the City argued that the double counting of the costs associated with the NID was result of a flaw in the LFAM model, this is incorrect. See AI Br. at p. 59. The City never made this argument. See City Initial Brief at pp. 61-62.

GCI and the City contend that Ameritech's explanation as to why it did not double count the costs of installing the NID are not credible and should be rejected by the Commission. GCI and the City will not repeat its substantive arguments here. GCI and the City have supplied language in its Brief on Exceptions. GCI and the City would only note that in Ameritech's Brief on Exceptions, Ameritech did not acknowledge that Ameritech witness Palmer admitted that his original study was flawed. See AI Ex. 10.1 at p. 18. Ameritech's explanation is an attempt to find additional costs that its original study could not support. Accordingly, Ameritech's recommended exception language should not be accepted.

3. Line Mix Assumption

To the extent that Ameritech's Brief on Exceptions implies that the City argued that the line mix assumption errors in its cost analysis was a function of its flawed LFAM model, this is incorrect. See AI Br. at p. 60. The City never made this argument. See City Initial Brief at p. 64.

Ameritech's argument in support of its line mix assumptions fail to address the fact that its analysis used data for the limited time frame of 1997-2003. See City Initial Br. at p. 64. This data includes only the higher priced growth lines for the year 2001, which is contrary to the fact that over the long term switches are replaced. Id. Thus, data for these years is not representative of the average forward-looking market price switch manufacturers would charge Ameritech. Accordingly, Ameritech's recommended exception language should not be accepted.

4. Revenue Ready Fees

To the extent that Ameritech's Brief on Exceptions implies that the City argued that the company's erroneous inclusion of revenue ready fees in its NAL LRSIC calculation was related to its flawed LFAM model, this is incorrect. See AI Br. at p. 61. The City never made this argument. See City Initial Brief at pp. 64-65.

Ameritech's argument fails to explain how costs that it readily admits relate to non-NAL "traffic engineering and provisioning functions" can be consistent with cost causation principles and properly included in the NAL LRSIC. See City Initial Br. at pp. 64-66. Accordingly, Ameritech's recommended exception language should not be accepted.

5. Billing Costs

To the extent that Ameritech's Brief on Exceptions implies that the City argued that the company's erroneous inclusion of certain billing costs in its NAL LRSIC calculation was related to its flawed LFAM model, this is incorrect. See AI Br. at p. 62. The City never made this argument. See City Initial Brief at pp. 66-67.

In its Brief on Exceptions, Ameritech argues that if NAL service was the only service ordered by a customer, all of the billing related costs would have to be incurred. AI Br. at p. 62. However, calculating the cost of service as if that were the only service provided is what is called a "stand alone" cost analysis. The "stand alone" cost is the ceiling for a proper price. It is the opposite of LRSIC. When several services are billed using the same envelope, that billing cost is no longer a cost caused by just the NAL, but is a cost that is shared by several services. See City Brief at pp. 66-67. Ameritech's costing would allow numerous competitive services that should pay their own way to "piggy-back" for nothing on NAL service. Such a scenario violates the Act's requirement that "in no case should rates or charges for noncompetitive telecommunications services include any portion of the cost of providing competitive telecommunications services ...." . See 220 ILCS 5/13-103. Accordingly, Ameritech's recommended exception language should not be accepted.

6. Capital Costs

To the extent that Ameritech's Brief on Exceptions implies that the City argued that the improper cost of capital used by Ameritech in its LRSIC studies was a function of its flawed LFAM model, this is incorrect. See AI Br. at p. 63. The City never made this argument. See City Initial Brief at p. 67.

In its Brief on Exceptions, Ameritech contends that it used a "forward-looking capital structure". AI Br. at p. 63. Ameritech conveniently ignores the fact that this Commission previously rejected the use of a similar equity to debt ratio, calling the 74.7% equity structure "a level that we believe is unprecedented in Commission telecommunications proceedings". See City Initial Br. at p. 67. Accordingly, Ameritech's recommended exception language should not be accepted by the Commission.

IX. SERVICE QUALITY – GOING FORWARD

A. Contrary to AI's Protests, the Service Quality Penalties Adopted in the HEPO Were Far From Excessive.

In its Brief on Exceptions, AI argues that the service quality penalties adopted in the HEPO are excessive. AI Brief on Exceptions at 28-29. Moreover, the Company complains that increases in penalties for service quality measures that the Company met over the course of the price cap plan and for newly adopted measures cannot be justified. Id. at 29. Amazingly, the Company even argues that increased penalties are not justified for the Installation Within 5 Days and OOS>24 Hours measures. Id. at 30. The Company opines that it was unable to meet the OOS>24 measure "only because of the unforeseen headcount losses that compromised installation and repair service generally – a problem separate from inadequate penalties." IBT Brief on Exceptions at 30.

IBT's continued refusal to acknowledge its service quality failings, in effect, underscores why increased penalties are so necessary in any plan approved in this docket: AI simply refuses to acknowledge its failings and, as evidenced in its continued poor performance in the OOS>24 measure, refuses to take the steps necessary to fix, once and for all, its inability to meet the measure. Simply put, adequate incentives in the form of stiff service quality penalties are included in the plan, AI will continue to perform badly while cashing in on its failure to invest in the form of record profits. The stiffer penalties adopted by the Commission must exceed the cost of investment needed to alleviate AI's abysmal service quality performance.

As both Staff and GCI parties have outlined in their Briefs, the Company's service quality failings during the life of the plan are well documented in this record. For example, the Commission was so outraged by the Company's poor service quality performance that it took the unprecedented action of calling IBT officials before the Commission to explain their abysmal performance in the areas of restoring service outages, installing network access lines and missing scheduled installation and repair appointments at customer premises.[1]

Moreover, as noted in CUB's Initial Brief, the Company's performance in critical customer service areas, such as installation within 5 days, trouble reports per 100 lines, responding promptly to customer calls to residential and repair call centers, and keeping POTS repair appointments has declined precipitously during the life of the Plan. See CUB Initial Brief at 37-42 and GCI/City Ex. 12.1, 12.2. and 12.3. Moreover, as fully documented in both CUB and Staff's Initial Briefs, the Company's assessments of its performance in the category of Installation within 5 Days has been grossly misleading given the fact that its computation of installation intervals includes vertical services installation requests (which do not require customer premise visits) and excludes installations of second and additional POTS lines. See CUB Initial Brief at 42-43, Staff Brief at 63-67.

AI's head-in-the-sand approach to acknowledging its service quality errors is highlighted by its insistence that its "conduct since 1999demonstrates that the existing penalties (including the $30 million penalty) are adequate to maintain reasonable performance." AI Brief on Exceptions at 30. This assertion is outrageous at best. See GCI Ex. 6.5, Schedule E-8 Revised; Staff Ex. 8.0 at 12. Even the ICC's decision to assess IBT an additional $30 million penalty for failure to achieve the OOS>24 benchmark in the year after the SBC/Ameritech merger was approved has not been enough to inspire improvement with respect to this measure. For the month of September, 2000, the Company reported an OOS>24 rate of 37.0%, more than seven times the benchmark level and the Company's worst monthly performance under the plan. Staff

[1] Chairman Mathias' questions to the Company and IBT's responses to those interrogatories can be found in a separate exhibit accompanying GCI/City witness Charlotte TerKeurst's Direct testimony, labeled as GCI/City Ex. 2.2 (IBT response to CUB data request 11.8).

Ex. 8.0 at 6. Moreover, the Company was assessed the $30 million penalty for failing to achieve the OOS>24 benchmark for the year 2000.

To a Company taking in more than $3 billion in revenues (see AI Ex. 7.2 (Dominak), p. 1), the HEPO's graduated penalty formula, which starts at $8 million and caps at $16 million, is hardly stringent. As noted in CUB's and the AG's Initial Briefs, the Company admitted during the SBC/Ameritech Merger proceeding (Docket No. 98-0555) that it costs the Company less to pay the service quality penalty adjustment than to invest the $30 million IBT estimates is needed to correct problems associated with meeting the OOS>24 measure. Docket No. 98-0555, Order of October 8, 1999 at 23, citing Tr. 817. Indeed, since the inception of the Plan, IBT has paid only about $29.5 million in cumulative service quality penalties and, as noted above, the OOS>24 benchmark was unmet for the year 2000.

In addition to arguing that its service quality problems have been limited to below-par performance in the OOS>24 category, the Company continues to stubbornly assert that it "has, without question, met this benchmark consistent over the life of the plan." AI Brief on Exceptions at 30. Of course, not only does the "question" exist that the Company failed this benchmark, there is undisputed evidence that the Company missed it each year during the life of the plan. Staff witness Sam McClerren confirmed in testimony that had the Company applied the correct definition of calculating installation performance with respect to solely POTS access lines, the Company would have missed the benchmark and been penalized each year of the price cap plan. Staff Ex. 8.0 at 10. Company witness Hudzik confirmed this when he admitted that excluding vertical services from the calculation significantly alters IBT's ability to meet the 90% within 5 days benchmark. Tr. 1934-1939. The Staff accordingly recommended that the Company be required to reduce its rates by $29.5 million, the amount that IBT would have paid in service quality penalties under the plan had the Commission known IBT calculated this performance measure in the incorrect manner it did. Staff Ex. 8.0 at 10; Staff Brief on Exceptions at 9-12. GCI urges the Commission to adopt this recommendation in its Final Order in this case.

AI also argues in its Brief on Exceptions that increased penalties for measures other than OOS>24 or newly adopted measures are inappropriate because there is no evidence that increased penalties are necessary to ensure compliance with these measures. AI Brief on Exceptions at 29. The Company asserts that its performance improved for six of the eight current benchmarks over the life of the plan. Id.

The Company's assessment should be rejected for several reasons. First, establishing differing penalty levels for different benchmarks would send the Company the wrong signal as to the importance assigned to each measure. The established measures represent the minimum performance criteria for a monopoly service carrier. The Company must approach each measure with equal interest and dedication. Second, establishing separate penalty levels for different annual measures invites the Company to reassign Company resources to achieving benchmarks that have a higher penalty, thereby risking failed compliance with other lower-penalty measures. Accordingly, maintaining a consistent penalty structure for each measure adopted in the plan – whether they are new or existing measures -- helps ensure that the Company approaches the maintenance of service quality as an integrated whole.

The Company's claims about improved service quality for various measures during the life of the plan should also be rejected. Contrary to the Company's claims, AI's substandard service quality performance has *not* been limited to the OOS>24 category. As noted above, the Company would have missed the Installation within 5 Days benchmark each year of the plan had it computed the measure correctly. In addition, its performance in the area of Trouble Reports per 100 lines has been of particular concern to Staff. See Staff Ex. 8.0 at 6. Moreover, the number of customer complaints against Ameritech, as revealed by the Commission's and the Company's own records have skyrocketed under alternative regulation. See CUB Initial Brief at 39-41, Staff Ex. 9.0 at 10-12.

Indeed, IBT's assertion that its service quality performance during the last five years is better than that achieved before the price cap plan began is pure deception. It is worth noting that in response to discovery promulgated by CUB, the Company indicated that data for the 1990 through 1994 time period was not available. See GCI/City Ex. 12.1. Yet, IBT somehow put together, and references in its Brief, a table in Mr. Hudzik's testimony that purportedly shows improvement in seven of the eight service quality benchmarks over the 1990 through 1999 time period. No explanation is provided as to where the 1990-1994 data came from. Accordingly, IBT's assessment should be ignored. Most importantly, the record evidence shows that service quality declined in several areas critical to monopoly customers, as discussed at pages 37-42 of CUB's Initial Brief.

In sum, Both Staff and GCI parties agree that IBT's service quality performance has declined precipitously during the tenure of the price cap plan. The Company's disingenuous representation of its service quality performance under the plan is refuted by the record and should be rejected.

B. AI's Interpretation of the Effect of HB 2900 On the Service Quality Provisions of the Plan Approved in this Docket Should be Rejected.

\In its Brief, AI argues that once rules are established by the Commission in response to HB 2900, provisions in the plan for individual customer penalties should be eliminated. AI Brief on Exceptions at 31-33. The Company argues, "At that point, additional penalties under the Alternative Regulation Plan will no longer be necessary, nor would they make good policy." Id. at 32.

AI's comments in this regard should be rejected. First, the new Section 13-712, assuming it is signed into law by the Governor, clearly states that the amounts listed as compensation levels for OOS>24 hours, failures to install within 5 days and failure to keep a scheduled installation or repair appointment are "minimum" levels. HB 2900, Section 13-712(d) and (e). Moreover, these are minimum standards and compensation levels for all telecommunications carriers providing basic local exchange service. Nothing in HB 2900 altered Section 13-506.1 of the Act, the provision that authorizes the adoption of alternative regulation for monopoly carriers. Section 13-506.1 makes clear that the Commission has the authority to tailor alternative regulatory provisions to fit the individual circumstances of a petitioning carrier. For example, Section 13-506.1(a) states that the Commission "is authorized to adopt different forms of regulation to fit the particular characteristics of different telecommunications carriers and their service areas." 220 ILCS 5/13-506.1(a). In addition, Section 13-506.1(b) states that the Commission " may modify or reject the carrier's proposed plan." 220 ILCS 5/13-506.1(b). The record in this case shows that AI failed to satisfy the statutory requirement that the alternative regulatory plan, "at a minimum…will maintain the quality and availability of telecommunications services." 220 ILCS 5/13-506.1(b)(6). That evidence alone justified increased penalties for the maintenance of service quality. Moreover, as the Commission recognized in its 1994 Price Cap Order, alternative regulation is an experiment of sorts, fraught with incentives to reduce expenditures for the maintenance of monopoly services in the interest of maximizing its income. Price Cap Order at 58. Clearly, that observation holds true today. The Commission, therefore, should reject AI's invitation to soften the terms of any plan adopted in this docket as a result of legislation that in no way affects the Commission's ability to fashion alternative regulatory plans.

Finally, the Company's reference to legal precedent discussing the goal of "limiting remedies to those necessary to compensate the aggrieved party" is inapposite to the circumstances in this docket. The decisions cited relate to damage awards to injured parties suing private businesses. Absent fraud, malice or gross negiligence, courts have no interest in awarding damages that exceed level incurred by plaintiffs. The instant docket, however, primarily is about establishing a regulatory framework for a monopoly telecommunications provider. The Commission's actions are dictated by a statute that permits the Commission to fashion a regulatory plan that it believes will incite appropriate behavior. Thus, the actions taken by the Commission in this proceeding are *not* just about providing remedies for aggrieved parties. The service quality penalty provisions adopted must, at a minimum, also achieve the goal of maintaining the quality and availability of telecommunications services. Accordingly, the cases cited by AI at page 32 of their Brief on Exceptions should be dismissed as irrelevant.

C. The Company's Criticism Of the HEPO's "Revision" Of The Installation Within 5 Days Standard Should be Rejected.

In its Brief on Exceptions, the Company characterizes the Examiners' conclusion that the Installation Within 5 Days benchmark should, over a period of years, reach the desired 95.44% benchmark as contrary to the HEPO's other conclusion that the Part 730 standard should be the benchmark. AI Brief on Exceptions at 33. The Company claims that because it has always included vertical services in its calculation of this measure, requiring it to achieve the more stringent benchmark is inappropriate. AI argues that to truly "maintain" service quality, the Commission should adopt the lower standard.

These protests should be dismissed. As GCI/City noted in their Brief on Exceptions, the Commission should retain the higher 95.44% benchmark level from the outset. Lowering the benchmark to the Part 730 level because AI has failed to meet even the minimum service quality standard on regular service installations is inconsistent with the statutory requirement that service quality be, at a minimum, maintained under the plan. Moreover, as noted earlier in this Brief, the Company's performance in the Installation Within 5 days category has been woefully inadequate in recent years. It is counterintuitive for the Commission to lower its expectations of the Company merely because AI has failed to meet minimum service quality standards – especially given the Commission's desire to establish a plan that incents the Company to improve service quality in this critical area.

Finally, the Commission should resist the invitation to lower its standards because AI chose to calculate this measure incorrectly over the years, and is apparently unwilling to make the investment necessary to meet this standard. To do so would invite similar bad behavior for other service quality measures.

Accordingly, GCI/City urge the Commission to retain the 95.44% benchmark for this service quality measure *from the outset.*

D. Contrary to the Company's Arguments, The Commission Should Adopt The GCI/City-Recommended Benchmark For the Missed Repair Commitments Measure.

In its Brief on Exceptions, AI complains that the HEPO inexplicably adopted Staff's proposed benchmark for the Missed Repair Commitments measure, rather than the Company-proposed level that encompasses a five-year performance average. AI Brief on Exceptions at 35. The Company complains that this finding is inconsistent with the HEPO's conclusion elsewhere in the Order that the Company's proposal to incorporate the 1994-1999 time frame when establishing benchmarks is the best proposal. Id. at 33-34.

In fact, both the Company- and Staff-proposed benchmark levels should be rejected. IBT provided no data for this measure for years preceding the adoption of the price cap plan. GCI/City Ex. 12.0 at 50. As a result, the Commission cannot be certain that adoption of a benchmark based on even the best year under alternative regulation will result in the maintenance, as opposed to the degradation, of service quality for this measure. Id. Also, the Company's internal target of 5% for % Missed Repair Commitments is markedly worse than its established target for % Missed Installation Commitments. This variance in target levels suggests that the Company places a higher priority on installing new service than repairing existing service. GCI/City Ex. 2.0 at 60.

The Company's performance data shows its % Missed Repair Commitments Due to Company Reasons increased from 5.21 percent in January of 2000 to 11.99 percent in June of 2000. Id. This stands in sharp contrast to the much lower % Missed Installation Commitment rates of between 1.18 percent and 1.72 percent in 2000, according to data in AI's NARUC report. GCI/City Ex. 2.0 at 58. Adoption of a 1 percent benchmark would ensure that IBT's inadequate performance results in financial consequences that escalate if service quality degrades further, and would help ensure that customers are not left waiting for their service to be repaired. IBT itself admits that it has achieved its internal benchmarks in the past.

E. Contrary to the Company's Protests, Separate Percent of Calls Answered Measures Should Be Established For Residential, Business and Repair Centers.

In its Brief on Exceptions, the Company argues that the final order should not include a measure for the Percent of Calls Answered. AI argues that such a measure is unnecessary because the measure that examines answering time is a more direct and precise method of ensuring prompt answering time at call centers. AI Brief on Exceptions at 37-38.

In its Brief on Exceptions, Staff clarifies that it is proposing a separate measure for Percent of Calls Answered. Staff recommends that a benchmark of 90 of all calls be answered, coupled with the 60-second benchmark it recommends for the Speed of Answer measure. Staff Brief on Exceptions at 23. Although Staff states that the Company should be required to report separately the percent of calls answered for business, residential and repair centers, it inexplicably declines recommending that the benchmark be applied separately for each of these categories. Id.

As noted in GCI/City's Brief on Exceptions, GCI/City recommends the inclusion of abandoned call measures for the residential, business and repair customer call centers, in accordance with Ms. TerKeurst's recommendations. As discussed by Ms. TerKeurst, these measures would be very useful in identifying any trend in the percent of calls that are abandoned because of excessive delays in response time. Staff witness Cindy Jackson pointed out in testimony that IBT data suggests that an increase in the average speed of answer results in an increase in the percent of calls abandoned by customers. Moreover, as detailed by Ms. TerKeurst, Company data shows that the percent of calls answered was markedly better for business than residential customer call centers. GCI/City Ex. 2.0 at 45. This phenomenon supports the establishment of separate Percent of Call Answered measures for the residential and business call centers. Measuring such data is equally important for repair call offices.

In short, the Percent of Call Answered measure provides another indicator of IBT's accessibility and responsiveness to customer inquiries and service needs. Although the Company has a 90% target level as its own internal measure, a 95% level should be established as the benchmark for each of these three measures. As noted by Ms. TerKeurst, IBT has been exceeding the 90% target benchmark. GCI/City Ex. 2.0 at 46. Thus, its use as a standard could result in a degradation of service. Instead, the benchmark should be based on IBT's actual performance to safeguard against erosion of service quality as required by Section 13-506.1(b)(6) of the Act. Moreover, use of such a standard would be consistent with the Commission's rationale for establishing a standard for the Company's % Installation Within 5 Days measure that was above the standard in Part 730 of the Commission's rules. See Alt. Reg. Order at 58.

Accordingly, the Commission should adopt three separate Percent of Call Answered standards, with a benchmark of 95 percent, for residential, business and repair call centers.

F. Contrary to the Company's Arguments, the Commission Should Adopt A Measure For Installation Repeat Reports, But Rename It POTS % Installation Repeat Trouble Reports.

In its Brief on Exceptions, AI continues to oppose the adoption of any measure for Installation Repeat Reports. AI Brief on Exceptions at 39. Like its previous briefs in this docket, the only reasoning the Company offers to support its position is its unsupported view that customers are only sensitive to repeat troubles associated with *repair* of telephone lines. Id. If the Commission adopts such a measure, however, AI point out that it erred when it criticized Ms. TerKeurst's "POTS % Installation Trouble Reports" data, supplied in GCI/City Ex. 12.1. The Company points out that the correct benchmark using historical data for 1998 and 1999 would be 4.41%. AI Brief on Exceptions at 40.

GCI/City concur with the HEPO's finding that an Installation Repeat Trouble Report Rate should be established. IBT already tracks the percent of new POTS installations that fail or are identified as improperly installed within seven calendar days of installation. GCI/City Ex. 2.0 at 57. This measure is computed as (count of installed POTS trouble rate within 7 calendar days of installation/total POTS installations) x 100. The Company's internal standard is that no more than five percent of POTS installations should experience trouble within seven calendar days. Id.

High installation trouble report rates should not be tolerated. Including a POTS % Installation Repeat Trouble Reports measure in the plan would help ensure that the myriad of new technicians the Company has been hiring (Tr. 1981, 1983-1985) would be trained to install service correctly the first time. GCI/Ex. 2.0 at 53.

As pointed out by GCI witness TerKeurst, customers have continuing concerns regarding the quality of IBT installations. The Company received a mean score of 86.5 points in the Ameritech Illinois Small Business Activation Survey and a mean score of 79.3 points in the Ameritech Illinois Small Business Assurance survey for performing installation work correctly the first time. GCI/City Ex. 2.0 at 53. Moreover, the Company received a mean score of 84.6 points in the Ameritech Illinois Consumer Activation survey and a mean score of 71.2 points in the Ameritech Illinois Consumer Assurance survey for performing installation work correctly the first time. Id.

The Company has maintained a POTS % Installation Trouble Report Rate ranging between 4.13 percent and 4.69 percent between 1998 and September 2000. It is important that the measure adopted for this service quality performance area make clear that it addresses *POTS and POTS only* problem installations. Ms. TerKeurst recommended that the Commission adopt a conservative benchmark of 5 percent. However, if, as the Company points out, the only available data support a benchmark of 4.41%, GCI/City will support such a measure. Accordingly, inclusion of the POTS % Installation Trouble Report Rate Within 7 Days measure with a 4.41% benchmark would help ensure that service quality is maintained (i.e., a reasonable amount of installations are done correctly the first time) on a prospective basis.

G. GCI/City Support Staff's Request for Increased Penalties

In its Brief on Exceptions, Staff argues many of the same points raised in GCI/City's Brief on Exceptions: namely that no deduction of "administrative expenses" and individual customer penalties from the overall, annual penalty amount paid by AI should be permitted (Staff Brief on Exceptions at 14) and that a cellular loaner program should be included as an option for customers failing to get a line installed or repaired by AI (Staff Brief on Exceptions at 13).

Staff also argues that the annual penalty amount should be increased by a $4 million per year any year that the Company misses an annual benchmark, rather than the $2 million per year additional amount for consecutive misses that the HEPO adopts. Staff Brief on Exceptions at 14. GCI/City support this proposed correction for the same reasons articulated by Staff: namely that the penalty level adopted must be sufficient to induce or compel AI to meet its service quality obligations.

GCI/City also support Staff's proposed language that would require the Company to explain on customer bills the basis for the credit, i.e. poor service quality. Id. at 15. GCI/City also support revising the HEPO's finding that the annual penalty amount should increase by an additional $4 million if a particular benchmark is not met by more than 5%, and continue to be applied for each 5% increment above the benchmark level. Id.

In addition, GCI/City support the notion that Company misses of the OOS>24 measure justify an additional $8 million per year missed, over and above the $30 million level established by the Commission in the Merger Order. Both the Company's continued failure to address this measure, along with the Company's admission that it would take an investment of some $30 million to rectify the problem justify adoption of this higher penalty level.

However, as GCI/City pointed out in their Brief on Exceptions, the $30 million penalty level was clearly adopted as an *additional* penalty, not to supplant any level in the alternative regulatory plan. As the Commission stated in its Price Cap Order:

> In subsequent full calendar year periods (including calendar year 2000), the Joint Applicants shall demonstrate compliance in the same manner currently used by the Commission and Ameritech Illinois to measure the Company's compliance with the OOS>24 service standard or face a one-time, $30 million assessment, *separate and apart from any annual rate reduction resulting from the service quality component of the company's Alternative Regulatory Plan.*

Merger Order at 24 (emphasis added). This highlighted language makes clear that the Commission intended that the $30 million penalty was a condition of approval of the Merger, and was to be assessed in addition to any service quality penalty included under alternative regulation.

Therefore, GCI/City urge the Commission to ensure that violations of the OOS>24 standard are punished with both the penalty mechanism approved in this Order ($8 million annually per miss, plus an *additional* $8 million for each additional annual miss of themeasure) *and* the $30 million penalty the Commission ordered as a condition in the Merger docket.

Finally, GCI/City wish to note, as pointed out by Staff, that the proposed Order fails to impose a customer-specific penalty for OOS misses until after 48 hours have passed. This is inconsistent with the language in HB 2900, which imposes a penalty after the 24th hour. In addition, as noted earlier in this Brief, the credit amounts listed in HB 2900 are "mimimum" amounts applicable to all monopoly carriers. In order to recognize the intrinsic incentive alternative regulation plans provide for companies to minimize investment in the interest of maximizing profits, the additional penalties proposed by Staff at page 16 of their Exceptions are reasonable and justified, and should be adopted.

H. Like Staff, GCI/City Oppose A Three-Year Phase-In Of Benchmarks.

In its Brief, Staff argues against the HEPO's three-year phase-in of compliance with benchmarks for new service quality measures. Staff Brief on Exceptions at 17. Instead, Staff argues an 18-month phase-in for new measures should be adopted. In GCI/City's opinion, however, any phase-in of the service quality benchmarks adopted in this Order should be rejected for a couple of reasons. First, the Commission did not believe such a phase-in was necessary when it first established the eight benchmarks that are a part of the existing service quality penalty mechanism. The notion that it could be financially affected by poor service quality performance was just as new to AI in 1994 as it is in 2001. Nevertheless, the Commission ordered no phase-in of benchmarks.

Second, all of the benchmarks adopted in the HEPO and proposed by GCI/City are service quality measures that the Company already tracks. Accordingly, there is no need to accommodate some alleged need to "prepare" its planning and budgeting cycles for the additional measures.

Accordingly, GCI/City urge the Commission to reject any kind of phase-in of the newly adopted service quality benchmarks.

I. Wholesale Service Quality Should Be Addressed in This Docket.

McLeodUSA and AT&T argue that wholesale service quality performance should be included as service quality measures in the Plan. McLeodUSA Brief on Exc.; AT&T Brief on Exc. at 8-10. GCI/City agree that the protections and incentives that the residential service quality measures and penalties provide should also be available to wholesale customers. Inadequate or unreliable wholesale service quality can undermine the development of retail competition, making the need to address it in this alternative regulation order compelling.

AT&T also addresses the four-basket structure, arguing that wholesale services should not be in the carrier basket, but in the retail basket. GCI/City support AT&T's position on this issue. See GCI/City Ex. 58-60.

X. CONCLUSION

Wherefore, GCI/City request that the Commission enter an Order consistent with the arguments and language presented in GCI/City's Brief on Exceptions, Exceptions, Erratas to the Brief on Exceptions and Exceptions and Reply Brief on Exceptions.

Respectfully submitted,

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